

Competition Taskforce
Via email: competitiontaskforce@treasury.gov.au

29 May 2024

Dear Competition Taskforce

Re: Worker non-compete clauses and other restraints

The Council of Small Business Organisations Australia (COSBOA) is the peak industry body representing 97 per cent of all Australian businesses. The ATO define a small business as one with an aggregated turnover of less than \$10 million and the ABS defines a small business as those with 0-19 employees. Depending on the definition used, the number of small businesses being referenced can vary.

Small businesses in Australia are faced with a multitude of complexities in running their businesses. From complex industrial relations reforms to changing privacy laws, to increased insurance, energy and wage costs. Small businesses do everything they can to protect their interests and the interests of their staff.

The following part of COSBOAs submission answers some of the questions raised in the Issues Paper

Discussion Questions

1. Common law restraint of trade and the *Restraints of Trade Act 1976 (NSW)* including suitability

Both the common law restraint of trade and the NSW legislative restraint of trade prevent a party from restricting another party's ability to engage in trade or employment unless there is reasonable interest of the parties involved or a reasonable public interest.

Non-compete clauses and other restraint of trade clauses are used by small businesses for a variety of reasons; to protect trade secrets and confidential information especially in industries where this is your comparative advantage, to safeguard client relationships, and to retain talent and protect investments undertaken in training where a lot of personal time and effort is given to upskill an employee.

COSBOA is sure the Taskforce is aware that in considering reasonableness, the Courts will assess whether there is a legitimate interest requiring protection and then whether the restriction protects the interest or does more than what is necessary. Where the restraint is

more than what is necessary, then the restraint is deemed unreasonable. More often than not, it will be the business who is wanting to enforce the restraint of trade that has the onus to prove there is a legitimate interest to protect.

Whilst small businesses do not always have large sums of money sitting to be used in legal cases, there are times when enforcement of the restraint is necessary. For example, where an employee holds a position that gives them access to particular confidential information and the industry they are operate in is small.

The question whether the current approach is suitable for all workers is questionable and will vary in answer depending on who is asked. Consideration has to be given to the restriction that is wanting to be enforced, the information held by the employee and their role. Businesses are likely to include non-compete clauses in contracts for all employees where the industry is small and there may only be a few operators. Alternatively, businesses may decide to only add in non-compete clauses for senior management and not other roles. COSBOA recommends that if a limitation on non-compete clauses is being considered, to ensure there is narrow application and to protect the genuine interests a business is trying to protect through the use of a non-compete clause.

2. Policy approaches in other countries

COSBOA understands that while on 23 April 2024, the US Federal Trade Commission (FTC) made its final rule to ban non-competes nationwide. The rule becomes effective 120 days after publication, therefore coming into effect on 4th September 2024.

The FTC ruling is being challenged currently in the court with injunctions being sought. However, COSBOA notes that the FTC ruling will make all non-competes ineffective after 4th September except for those senior executives who have non-competes currently in place. Senior executives earning more than \$151,164 and who have non-compete clauses currently in their employment contracts are still valid (and will be even after the effective date).

As mentioned previously by COSBOA in consultation with the Taskforce members, comparison of the economic benefits of banning non-competes in the US with Australia is not very useful. Australia's economy and population is significantly smaller. Of the 7,000 businesses interviewed regarding restraint clauses, ABS finds that small businesses had the lowest use of non-compete clauses (20.2 per cent) with larger businesses (more than 1,000 employees) used non-compete clauses 40 per cent of the time. Only one percent of Australian businesses said that a potential employee had turned down their job offer because of a non-compete clause.

The UK proposal to limit non-competes to 3 months is an alternative that is more suited than a blanket ban, however, there have been no updates on proposed legislation since the proposal in 2023.

Following a time-limit ban to non-competes, the Netherlands' approach to limit non-competes to 12 months alongside inclusion of geographical scope, a written justification for

the business interest may be more appropriate in the Australian context. However, the Netherlands have also included a provision for mandatory compensation for the employee when invoking the non-competition clause, this is at least 50 per cent of the employee's monthly salary. COSBOA is certain that small businesses will not support the inclusion of mandatory compensation for an employee of a small business and recommends the Taskforce not consider mandatory compensation as an option.

3. Non-solicitation of co-workers, clients and other business contacts

Some COSBOA members note that non-solicitation clauses are used to protect the small businesses from staff members and clients being poached. The enforceability of non-solicitation clauses (including non-competes) were seen as having more of a deterrent effect than something that is enforceable (or worthwhile trying to enforce given timeliness and cost). However, even with the possibility that a clause may not be enforced, it was important to ensure that businesses were able to continue operating in certain geographical locations without the loss of clientele when a staff member moves.

Non-solicitation clauses can frequently be seen in the finance, hairdressing and allied healthcare settings. The use of these clauses is not limited to just the aforementioned industries.

Additionally, small businesses may use non-solicitation clauses for co-workers to protect the loss of a skilled workforce. It is not only acute for start-ups/new firms. As previously mentioned, small businesses are already struggling with skilled shortages and these clauses are used to safeguard a businesses' investment in its workforce, its confidential information and avoid disruptions to client relationships.

4. Non-disclosure clauses

Small businesses use non-disclosure clauses in employment contracts even where protections such as s183 of the *Corporations Act 2001* are available because it provides tailored protection for the business whilst also clearly notifying an employee of their obligations. Some small businesses may use standard template employment contracts, and some small businesses use tailored templates which identify and stipulate the type of confidential information an employee may be privy to and remind them of their obligation to keep this information confidential.

It also provides small businesses employers with the ability to clearly stipulate in the contract that breach of the non-disclosure clause may result in termination of employment and/or damages being sought in court.

The combination of s183 alongside the use within the employment contract provides additional security for a small business owner that finds an employee using confidential information for personal gain outside of their employment.

It is COSBOA's view that the use of non-disclosure clauses does not impact worker mobility where the non-disclosure clause is written in specific terms related to confidential information held by the business that is not readily available publicly. The skills and knowledge that an employee holds and develops at a place of employment can easily find them a new job, however, the previous employer's confidential information regarding intellectual property or finances etc do not impact an employee's mobility.

5. Restraint of trade clauses

COSBOA is of the view that restraint of trade clauses are appropriate where an employee has access to confidential information that could be used if engaging in part-time work within the same area. Similar to how the public service requires approval if an employee is engaging in a secondary or voluntary job, it may be appropriate in some industries for an employee to be limited from engaging in part-time work within the same industry where one job provides access to information that can result in personal gain (e.g. an individual working at the ATO should not be assisting a family member at their accounting firm as confidential information may be leaked, even if inadvertently.)

Restraint of trade clauses have to be determined on a per case basis depending on the industry in which one is operating in.

6. COSBOA member commentary

COSBOA spoke to members in writing this submission and the following general comments were made:

- Most members noted that non-compete and non-solicitation clauses were seen as having more of a deterrent effect than something that is enforceable (or worthwhile trying to enforce given timeliness and cost).
- Banning non-compete/restraint of trade clauses can impact the capital value of a small business (specifically where another business is wanting to buy a small business, key personnel with no restrictions can be deemed as a risk to the potential buyer).

Conclusion

COSBOA has been supportive of the Government's Competition Review and has always said that the Australian economy is best served by markets that comprise of big and small businesses. This includes mobility of staff to ensure even the smallest of businesses are given opportunities to grow into big businesses. However, whilst the Taskforce notes that non-competes and other restraints are impacting employee mobility, wages and productivity, there are significant other improvements that can be made than limiting some protections employers put in place to preserve their business.

Fewer Australians are changing jobs in the last few years due to a variety of reasons such as economic uncertainty and the flow on effects of the pandemic. The way in which people work has changed drastically and government needs to consider alternate ways to increase innovation and productivity within the Australian community.

Small businesses are also becoming less innovative given the complex regulatory frameworks they have to operate in; this therefore also impacts start-ups to form given the regulatory burden of running a business. Technological adaptation and weak business investment are also impacting innovation, productivity and therefore competition in Australia.

COSBOA recommends the Taskforce also consider how Government can assist small businesses by creating a more favourable environment to run a business.

COSBOA welcomes any further consultation the Taskforce may have on this topic, or any topic related to how the small business environment can be improved.

Yours sincerely,

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